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Department of the Treasury  
Washington, DC 20224

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Refer Reply To:  
CC:TEGE:EOEG:EO1  
PLR-109042-11

Date:  
June 29, 2011

City:

Trust:

Trustee:

Administrator:

## Agreement:

Year:

State:

Statute:

Dear

This letter responds to a letter from your authorized representative dated February 22, 2011, submitted on behalf of the City, requesting rulings that the income from the Trust is excludable from gross income under § 115 of the Internal Revenue Code. The City represents the following facts.

## FACTS

The City was formed in Year and is a political subdivision of the State. It contributes an agreed-upon amount monthly for payment of health insurance premiums for its employees and retirees under the Statute. The City has agreed also to pay additional amounts for employees' and retirees' health insurance coverage under a health reimbursement arrangement.

The City has established the Trust to fund payment of post-employment medical insurance premiums for eligible retirees and has appointed Trustee and Administrator to serve accordingly.

The Trustee will accept and account for contributions from the City, will keep the contributions and earnings separate from the City's operating funds, will invest and reinvest the contributions according to instructions from the Administrator, and will pay out benefits for the exclusive benefit of the City's eligible employees and retirees.

Contributions to the Trust are irrevocable and are to be used solely to provide benefits for beneficiaries and to pay expenses of administering the trust. The Trust income will consist of contributions from the City plus investment earnings. Private interests will neither participate in, nor benefit from, the operation of the Trust other than as providers of goods or services for reasonable compensation.

The Agreement may be amended or terminated according to its terms by either the Administrator or the City. Upon termination of the Trust, and after satisfaction of all liabilities to employees or former employees and their beneficiaries, any remaining balance will be distributed to the City, to an entity whose income is excludable under § 115, or to a "qualified trust" as described in the Agreement.

## LAW AND ANALYSIS

Section 115(1) provides that gross income does not include income derived from any public utility or the exercise of any essential government function and accruing to a state or any political subdivision thereof.

In Rev. Rul. 77-261, 1977-2 C.B. 45, income from an investment fund, established under a written declaration of trust by a state, for the temporary investment of cash balances of the state and its participating political subdivisions, was excludable from gross income for federal income tax purposes under § 115(1). The ruling indicated that the statutory exclusion was intended to extend not to the income of a state or municipality resulting from its own participation in activities, but rather to the income of a corporation or other entity engaged in the operation of a public utility or the performance

of some governmental function that accrued to either a state or municipality. The ruling points out that it may be assumed that Congress did not desire in any way to restrict a state's participation in enterprises that might be useful in carrying out projects that are desirable from the standpoint of a state government and which are within the ambit of a sovereign properly to conduct.

In Rev. Rul. 90-74, 1990-2 C.B. 34, the income of an organization formed, funded, and operated by political subdivisions to pool various risks (casualty, public liability, workers' compensation, and employees' health) was excludable from gross income under § 115. In Rev. Rul. 90-74, private interests neither materially participated in the organization nor benefited more than incidentally from the organization.

The Trust was established and is maintained by the City to fund health insurance premiums for its retired employees and their beneficiaries. Providing such health benefits to former public employees constitutes the performance of an essential governmental function within the meaning of § 115(1). See Rev. Rul. 90-74 and Rev. Rul. 77-261.

The funding and payment of retiree health insurance premiums through the Trust satisfies the obligation of the City to provide such benefits; thus, the income of the Trust accrues to the benefit of the City, which is a political subdivision of the State. No private interests participate in, or benefit from, the operation of the Trust, other than as providers of goods and services. Any amounts remaining in the Trust after all liabilities have been satisfied shall be distributed to the City, a § 115 entity, or a qualified trust as defined in the trust's governing document. In no instance will any remaining assets be distributed to an entity other than the State, a political subdivision, or a § 115 entity. The benefit to retired employees is incidental to the public benefit. See Rev. Rul. 90-74.

### CONCLUSION

Based solely on the facts and representations submitted by the City, including the proposed First Amendment to the Agreement, we conclude that the income of the Trust is derived from the exercise of essential governmental functions and will accrue to a state or a political subdivision thereof for purposes of § 115(1). Consequently, we rule that, as of the date the First Amendment is adopted, the income of the Trusts is excludable from gross income under § 115(1).

Except for the specific ruling above, no opinion is expressed or implied regarding the federal tax consequences of the facts of this case under any other provision of the Code. Specifically, no representation is made that contributions or premiums paid on behalf of, or benefits received by, employees, former employees, retirees, spouses, dependents, or others will be tax-free. This ruling concerns only the federal tax treatment of the Trust's income and may not be cited or relied upon as to any matter relating to the taxation of accident or health contributions or benefits.

Under a power of attorney on file with this office, we are sending a copy of this letter to your authorized representative.

This ruling is directed only to the taxpayer who requested it. According to § 6110(k)(3), this ruling may not be used or cited as precedent.

Sincerely,

SYLVIA HUNT  
Assistant Chief  
Exempt Organizations Branch 2  
Office of Division Counsel /  
Associate Chief Counsel  
(Tax Exempt & Government Entities)

enclosures: copy for § 6110 purposes

cc: